

REPORT OF EXAMINATION
OF THE
FIRST AMERICAN TITLE INSURANCE COMPANY
AS OF
DECEMBER 31, 2004

Participating State
and Zone:

California

Filed June 29, 2006

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Los Angeles, California
May 5, 2006

Honorable Alfred W. Gross
Chairman of the NAIC Financial
Condition (EX4) Subcommittee
Commissioner of Insurance
Virginia Bureau of Insurance
Richmond, Virginia

Honorable Gary L. Smith
Secretary, Zone IV-Western
Director of Insurance
Department of Insurance, State of Idaho
Boise, Idaho

Honorable John Garamendi
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Chairman, Director and Commissioner:

Pursuant to your instructions, an examination was made of the

FIRST AMERICAN TITLE INSURANCE COMPANY

(hereinafter also referred to as the Company) at its home office located at One First American Way, Santa Ana, California 92707.

SCOPE OF EXAMINATION

The previous examination of the Company was made as of December 31, 2000. This examination covers the period from January 1, 2001 through December 31, 2004. The examination was made pursuant to the National Association of Insurance Commissioners' plan of examination. The examination included a review of the Company's practices and procedures, an examination of management records, tests and analyses of detailed transactions within the examination period, and an evaluation of the assets and a determination of liabilities as of December 31, 2004, as deemed necessary under the circumstances.

In addition to those items specifically commented upon in this report, other phases of the Company's operations were reviewed including the following areas that require no further comment: fidelity bonds and other insurance; officers', employees' and agents' welfare and pension plans; corporate records; growth of company; business in force by states; loss experience; and sales and advertising.

Certain phases of the examination were completed at branch offices located in Boston, Massachusetts; Portland, Oregon; Tallahassee, Florida; Fairfax, Virginia; and Warrenville, Illinois.

COMPANY HISTORY

The Company is authorized to issue 5 million shares of common stock at a par value of \$100 per share. There were 2 million shares of common stock outstanding as of December 31, 2004. The First American Corporation, owns 100% of the outstanding shares of common stock.

On June 30, 2002, the Company issued a stock dividend of 1 million shares of common stock with a par value of \$100 per share to its parent, The First American Corporation (FAC).

MANAGEMENT AND CONTROL

The Company is a wholly-owned subsidiary of The First American Corporation (FAC). The following is a list of the Company's direct subsidiaries and percentage of ownership interest:

<u>Subsidiaries</u>	<u>Percent of Ownership</u>
Albany County Title	100.00%
All New York Title Agency Corporation	100.00%
Allegiance Title	100.00%
Allied Trustee Services, Inc.	100.00%
Androscoggin	100.00%
ATI Title	100.00%
Atlantic Title Company	100.00%
Attorney's Abstract, Inc.	100.00%
Beaumont Title	100.00%

<u>Subsidiaries</u>	<u>Percent of Ownership</u>
Brokers Title	100.00%
Burton Abstract & Title Company	100.00%
C.T.P., Inc.	8.34%
Cahaba Title, Inc.	28.96%
Caldwell County Abstract Company, Inc.	100.00%
California Title	30.00%
Campbell County Abstract Company	64.08%
Capitol Title	27.50%
Carriage Escrow	49.00%
Censtar Title Insurance Company	55.00%
Columbian National Title Insurance Company	100.00%
Columbian Title of Johnson County, Inc.	100.00%
Columbian Title of Kansas City, Inc.	100.00%
Columbian Title of Topeka, Inc.	100.00%
Columbian Title of Witicha, Inc.	100.00%
Connecticut Title Services	100.00%
Converse Land Title Company	91.40%
Cornerstone Title Company	51.00%
Eagle Title & Abstract Corporation	100.00%
Eastern Abstract	20.93%
Equity Title	25.00%
Fidelity Abstract Title of New Jersey	20.00%
Fidelity Title and Guaranty Company	100.00%
First American Abstract	100.00%
First American Affiliates	100.00%
First American Equity Loan Service	100.00%
First American Homebuyers Protect Corporation	92.26%
First American Homebuyers Protection of Delaware	50.00%
First American Title & Trust Company Oklahoma	100.00%
First American Title and Abstract (OK)	100.00%
First American Title Company of Florida, Inc.	100.00%
First American Title Company of Hawaii	80.00%
First American Title Company of Idaho	100.00%
First American Title Company of Illinois	100.00%
First American Title Company of Los Angeles	100.00%
First American Title Company of Marin	100.00%
First American Title Company of Nevada	100.00%
First American Title Company of Waco dba First Title	100.00%
First American Title Guaranty Agency of Cheyenne	98.16%
First American Title Guaranty Agency of Crook County	91.34%
First American Title Guaranty Holding Company	100.00%
First American Title Guaranty of Carbon County	88.70%

<u>Subsidiaries</u>	<u>Percent of Ownership</u>
First American Title Guaranty of Sublette County	81.03%
First American Title Holding Company (formerly FA Title)	24.12%
First American Title Insurance Agency of Mohave	96.53%
First American Title Insurance Agency of Utah, Inc.	100.00%
First American Title Insurance Agency, Inc./Navaho	100.00%
First American Title Insurance Company of Australia Pty	100.00%
First American Title Insurance Company of Kansas	100.00%
First American Title Insurance Company of New York	100.00%
First American Title Insurance Company of North Carolina	100.00%
First American Title Kansas Agency, Inc.	100.00%
First American Title Missouri Agency	100.00%
First American Transportation Insurance Company	100.00%
First Australian	100.00%
First Canadian Title Company, Ltd.	100.00%
First Canadian Title Insurance Company	100.00%
First Hong Kong Title	100.00%
First States	100.00%
First Title PLC dba First American Title Insurance Company	100.00%
Fremont County Title Company	100.00%
General Land Abstract Company	100.00%
Goshen County Title Company	76.44%
Greater Louisiana Title Insurance Company	100.00%
Guarantee Abstract Title (MA)	100.00%
Guaranty Title Company, Inc. of Maine	100.00%
Hi-Tech Title Solutions Inc.	30.00%
Inland Empire Service Corporation	100.00%
Investors Title Company	19.99%
Island Title Corporation	60.00%
Johnson County Title Company Inc.	51.00%
Land Title Insurance Company of St. Louis	100.00%
Massachusetts Abstract Company Inc.	100.00%
Memphis Title Company	100.00%
Metropolitan Title	100.00%
Mid Valley Title and Escrow Company	59.59%
Midland Title Agency of NW Ohio	100.00%
Midland Title Security Inc.	100.00%
National Land Title of Tarrant, Inc.	100.00%
New York Abstract Company	100.00%
Ohio Bar	100.00%
Ohio Title Corporation	100.00%
Pacific Northwest Title Holding Company	100.00%
Penn Attorneys Title Insurance Company	100.00%

<u>Subsidiaries</u>	<u>Percent of Ownership</u>
Pilgrim Title Insurance Company – Rhode Island	35.00%
Pioneer Agency	100.00%
Port Lawrence Title and Trust Company	100.00%
Priority Title	51.00%
Republic Title of Texas Inc.	100.00%
Security First Title Associates	100.00%
Security Land Title of Omaha	45.19%
Settlers Title Agency Inc.	100.00%
Shoshone Title	53.72%
Signature Title	100.00%
Skagit County Title Company	11.59%
TA Holdings, Inc.	100.00%
Teton Land Title Company	92.14%
The Title Security Group	100.00%
Title Insurance Company of Oregon	100.00%
Title Partners of America	100.00%
Twin City Title	100.00%
Universal Title Company	100.00%
Warranty Title	100.00%
Washakie Abstract Company	100.00%
Western National Title Insurance Company	100.00%
Wyoming Land Title Company	60.48%

The management of the Company is vested in a nineteen-member board of directors. A listing of the members of the board and principal officers serving on December 31, 2004 is as follows:

Directors

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Parker S. Kennedy Santa Ana, California	Chairman of the Board and Chief Executive Officer The First American Corporation Chairman of the Board First American Title Insurance Company
Donald P. Kennedy Santa Ana, California	Chairman Emeritus The First American Corporation Vice Chairman of the Board First American Title Insurance Company
Gary J. Beban Northbrook, Illinois	Senior Executive Managing Director CB Richards Ellis, Inc.
James D. Chatham Alpharetta, Georgia	President and Chief Executive Officer Chatham Holdings Corporation
The Honorable William G. Davis Brampton, Ontario Canada	Counsel Torys, LLP
Craig I. DeRoy Rolling Hills Estates, California	President The First American Corporation Vice President First American Title Insurance Company
Dr. James L. Doti Villa Park, California	President and Donald Bren Distinguished Chair of Business and Economics Chapman University
Lewis W. Douglas, Jr. Denver, Colorado	Chairman Stanley Energy, Inc.
Paul B. Fay, Jr. Woodside, California	President The Fay Improvement Company

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
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Gary L. Kermott
Dana Point, California

Executive Vice President
The First American Corporation
President
First American Title Insurance Company

Thomas A. Klemens
San Clemente, California

Senior Executive Vice President and
Chief Financial Officer
The First American Corporation
Vice President
First American Title Insurance Company

John W. Long
Tierra Verde, Florida

President and Chief Executive Officer
First Advantage Corporation

Frank E. O'Bryan
Newport Beach, California

Private Investor

James M. Orphanides
Princeton, New Jersey

Regional Vice President
First American Title Insurance Company
President and Chief Executive Officer
First American Title Insurance Company of
New York

Roslyn B. Payne
San Francisco, California

President
Jackson Street Partners, Ltd.

David Van Skilling
Palm Desert, California

Private Investor

Herbert B. Tasker
Orinda, California

Mortgage Industry Consultant

Virginia M. Ueberroth
Laguna Beach, California

Chairman
Ueberroth Family Foundation

Martin R. Wool
Bell Canyon, California

President and Chief Executive Officer
First American Home Buyers Protection
Corporation

Principal Officers

<u>Name</u>	<u>Title</u>
Parker S. Kennedy	Chairman of the Board
Donald P. Kennedy	Vice Chairman of the Board
Gary L. Kermott	President
Curt A. Caspersen	Senior Executive Vice President
John M. Hollenbeck	Senior Executive Vice President
Dennie L. Rowland	Senior Executive Vice President
John N. Casbon	Executive Vice President
Mark R. Arnesen	Secretary
Craig I. DeRoy	Vice President
Thomas A. Klemens	Vice President
Thomas R. Wawersich	Chief Financial Officer
Timothy P. Sullivan	General Counsel

Intercompany Agreements:

Cost Allocation Agreement: FAC and the Company provide administrative services, facilities and benefits to First American Title Insurance Company of New York (the “Insurance Company”). The cost of service is determined by FAC and the Company and allocated to the Insurance Company for payment within 90 days from the date of allocation.

Management Agreement: The Company provides management and office services to First American Title Insurance Company of Kansas (FATKS). The Company provides an invoice after the close of each month on the cost incurred by the Company to FATKS. The cost cannot exceed \$10,000 per month. FATKS pays all invoices within ten (10) days of receipt.

Cross Indemnity Agreement: The following are parties to the agreement: The Company, First American Title Insurance Company of Oregon, Censtar Title Insurance Company, Land Title Insurance Company of St. Louis, First American Title & Trust Company of Oklahoma, Mortgage Guarantee and Title Company, The Port Lawrence Title & Trust Company, and Massachusetts Title Insurance Company. The parties to the agreement jointly and severally indemnify each other for title losses and claims tendered by persons or entities named as insureds under policies of title insurance issued by any of the parties to the agreement subject to the financial ability to pay determined in the most recent annual or quarterly statements filed by the parties to the agreement

with the insurance regulatory agency of its state of incorporation. The amount of indemnity cannot exceed fifty percent (50%) of any party's property or business.

Underwriting Agreement: The Company maintains an Underwriting Agreement with First American Title Company (FATCO) for the purpose of issuing title insurance policies in the following counties of California: Alpine, Amador, Calaveras Del Norte, El Dorado, Fresno, Humboldt, Imperial, Kern, Kings, Lake, Lassen, Los Angeles, Madera, Marin, Mariposa, Mendocino, Monterey, Nevada, Orange, Placer, Plumas, Riverside, Sacramento, San Bernardino, San Diego, San Francisco, San Luis Obispo, San Mateo, Santa Barbara, Santa Cruz, Shasta, Sierras, Sonoma, Stanislaus, Sutter, Trinity, Tulare, Tuolumne, Ventura, Yolo and Yuba. FATCO remits to the Company on or before the 15th day of each calendar month an amount equal to five percent (5%) of the total amount of fees for title policies issued through its offices during the preceding calendar month. The Company is liable for claims made under title policies issued by FATCO, subject to a deductible amount of \$5,000 paid by FATCO.

Tax Allocation Agreement: The Company and its affiliates are parties to a Tax Allocation Agreement dated December 15, 1994 with its ultimate parent, First American Corporation (FAC). FAC files consolidated federal income tax returns and pays estimated consolidated federal income taxes due. Each member pays to FAC its estimated separate federal income tax liability. The allocation of federal income tax liability is based on the percentage that the separate federal tax liability bears to the sum of the tax liability for all members. The members of the group that incurred losses or other tax benefits that have been utilized by the group to reduce consolidated federal tax liability are compensated for the use of the benefits. Any excess of the amount paid over the allocated liability is paid back by FAC within ninety (90) days after the due date, including extensions of the consolidated federal return.

TERRITORY AND PLAN OF OPERATION

As of December 31, 2004, the Company is licensed to conduct title insurance business in the District of Columbia and in all states, except Iowa, Kansas and New York. The Company is also licensed in Guam, Puerto Rico, the U.S. Virgin Islands, Canada, Hong Kong, South Korea, and the Bahama Islands.

During the examination period, the majority of the premiums were written in California (26.21% in 2004), Florida (9.11% in 2004) and Michigan (4.45% in 2004). The Company's direct premiums written in 2004 were \$3.4 billion of which \$531.5 million were produced through direct operations, \$2.0 billion through non-affiliated agencies and \$804.3 million through affiliated agencies. California premium writings totaled \$883.9 million or 26.21% of the total premiums written.

The Company is licensed to write residential and commercial title insurance policies. Title insurance policies insure the interests of owners and their lenders in the title to real property against loss by reason of adverse claims to ownership of, or to defect, liens, encumbrances or other matters affecting such title that existed at the time a policy is issued and that were not excluded from the policy coverage. The Company also provides escrow and other services to real estate property buyers and mortgage lenders.

Title policies are issued by the Company on a direct basis, by underwritten title companies, and through title agents on behalf of the Company on an indirect basis. Some underwritten title companies and other title agents are partially or wholly-owned by the Company. The underwritten title companies, and other title agents, retain from 60% to 95% of the title insurance premiums when they place the business with the Company. The amount of retention depends on local regulations or practices and on whether the pricing is all inclusive or divided between the so-called "risk portion" of the premium and the so-called "work portion", such as search, examination and policy preparation.

REINSURANCE

Assumed

The Company assumes business from subsidiaries and affiliates as well as from unaffiliated companies. In the ordinary course of business, orders for large policies are often received with the applicant directing the underwriting company to cede a portion of the risk to other insurers for specific amounts. The Company is one of the nation's largest title insurers and as a result, receives a great amount of directed reinsurance on a facultative basis. It also has treaty reinsurance, which is automatic coverage with several companies. The automatic reinsurance agreements as of December 31, 2004 are as follows:

Subsidiaries and Affiliates:

<u>Company</u>	<u>Retention</u>
Censtar Title Insurance Company	\$ -0-
First American Title Insurance Company of Australia	\$ 100,000
First American Title Insurance Company of New York	\$ -0-
First American Title Insurance Company of North Carolina	\$ 500,000
First American Title Insurance Company of Oregon	\$ 5,000,000
First American Title Insurance Company - PLC	£ 20,000
Land Title Insurance Company of St. Louis	-0-
Massachusetts Title Insurance Company	\$ 3,500
Pacific Northwest Title Insurance Company	\$ 2,000,000
T.A. Title Insurance Company	\$ 500,000
Western National Title Insurance Company	\$ 200,000

Unaffiliated Companies:

<u>Company</u>	<u>Retention</u>
Atlantic Title Insurance Company	\$ 100,000
Attorneys' Title Guaranty Fund, Inc.	\$ 250,000
Commerce Title Insurance Company	\$ 5,000
Dreibelbiss Title Insurance Company	\$ 75,000
<u>Company</u>	<u>Retention</u>

Guardian Title Insurance Company	\$ 100,000
Investors Title Insurance Company	\$ 2,750,000
National Attorney's Title Assurance Fund	\$ 100,000
New England Title Insurance Company	\$ 100,000
North American Title Insurance Company	\$ 2,500,000
Northeast Investors Title Insurance Company	\$ 250,000
Northern Counties Title Insurance Company	\$ 1,000,000
The Security Title Guarantee Corporation of Baltimore	\$ 1,000,000
Title Resources Guaranty Company	\$ 1,500,000
Westcor Land Title Insurance Company	\$ 100,000

As of December 31, 2004, the Company assumed business from affiliates with policy liabilities totaling \$26.6 billion and reinsurance premiums of \$1.2 million. The Company also assumed business from non-affiliates with policy liabilities totaling \$16.6 billion and reinsurance premiums of \$6.4 million. The aggregate assumed reinsurance liability totaled \$43.2 billion and reinsurance premiums received amounted to \$7.6 million.

Ceded

The Company cedes its excess risk on a facultative basis. The total ceded reinsurance liability to affiliates and non-affiliated insurers amounted to \$14.2 billion with \$9.0 million total ceded reinsurance premiums paid as of December 31, 2004. The Company's maximum voluntary risk retention is \$400 million each risk. The Company remains contingently liable for title insurance losses and other claims associated with ceded reinsurance, in the event the reinsurer is unable to satisfy its contractual obligations.

Captive Reinsurance

The Company has executed a Consent Order with the Colorado State Division of Insurance (COSDI) wherein COSDI asserts that the Company participated in an industry-wide practice of offering captive reinsurance arrangements to residential homebuilders with captive reinsurance companies. The parties involved were then paid a portion of the insurance premium as reinsurer. The COSDI

has asserted that this practice was a referral payment and unfair business practice in violation of Colorado law. In settling the matter, the Company has agreed to cease participating in captive reinsurance arrangements of this nature without admission of liability or wrongdoing.

The Company has similar reinsurance arrangements in other states, including California, and it has determined that the entire amount of premiums paid pursuant to its captive reinsurance arrangements nationwide has been \$24 million in total since inception.

In 2005, the Company terminated all its captive reinsurance arrangements with those parties, and has unilaterally and voluntarily paid the affected policyholders the allocated portion of the reinsurance premium paid to the captive reinsurance participants to avoid the appearance of improper conduct by the Company or its homebuilder reinsurance in connection with the captive reinsurance arrangements.

ACCOUNTS AND RECORDS

Escrow Accounts

A review was made of the Company's escrow accounts as of December 31, 2005. The review was performed at various branch offices of the Company. Based on the review, which included the escrow trial balance and reconciliations, it was noted that the various branches were not consistent in the method in which escrow balances and related liabilities were recorded in its corporate trial balance. It was recommended that the Company implement a procedure regarding the recording of the different branch offices' escrow balances and related liabilities in its corporate trial balance for both the interest and non-interest bearing accounts. As a result, the Company implemented a procedure for all regional branches that the book (trial balances) escrow balances will be reported in its corporate trial balance for all interest and non-interest bearing accounts.

The review also included a review of sample files selected from the various branch offices' escrow trial balances. The review of sample files included the following: cash receipt and disbursement

instructions and its implementation, review of escrow instructions and its implementation as agreed upon by the seller and buyer, verification of county location and inclusion of a pro-forma or title insurance policy/coverage on the property being transacted. Based on the review of the sample files, the Company was found to be in compliance with the California Insurance Code Section (CICS) 12413.1, escrow funds were not being disbursed until the day on which funds were made available to depositors. However, it was noted that there were some closed escrow accounts with balances in its escrow trial balance. It is recommended that the Company resolve all the outstanding escrow balances before it closes the escrow account and escheat undisbursed escrow funds as unclaimed property in accordance with the requirements of each state.

Custodial Agreement

The present custodian for the Company's securities is First American Trust, FSB. The Company is not in compliance with CICS 1104.9 because the custodial agreement did not meet the requirements of CICS 1104.9 (d). In 2003, the Company submitted an application for First American Trust, FSB, as a qualified custodian pursuant to CICS 1104.9(a)(1). The application was not in compliance with CICS 1104.9(a) due to the lack of a credit rating as required by the California Department of Insurance (CDI). As a result, the Company withdrew its application in 2004. It is recommended that the Company comply with CICS 1104.9 by utilizing a qualified custodian for its securities.

FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of December 31, 2004

Underwriting and Investment Exhibit for the Year Ended December 31, 2004

Reconciliation of Surplus as Regards Policyholders
from December 31, 2000 through December 31, 2004

Statement of Financial Condition
as of December 31, 2004

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$ 29,947,227	\$	\$ 29,947,227	
Stocks: Preferred stocks	6,226,196	5,170,096	1,056,100	
Stocks: Common stocks	652,506,861		652,506,861	(1)
Mortgage loans on real estate	34,786,622		34,786,622	(2)
Real estate - properties occupied by the company	80,447,072		80,447,072	
Real estate - properties held for the production of income	2,044,172		2,044,172	
Cash, cash equivalent and short-term investments	555,758,091		555,758,091	
Other invested assets	97,267,066	37,828,026	59,439,040	
Investment income due and accrued	3,357,275		3,357,275	
Premiums and considerations – uncollected premiums and agents' balances in the course of collection	80,830,984	(1,150,205)	81,981,189	
Net deferred tax asset	97,538,834	71,715,829	25,823,005	
Electronic data processing equipment and software	185,952	185,952		
Receivables from parent, subsidiaries and affiliates	213,218,486	41,122,653	172,095,833	(3)
Other assets nonadmitted	140,450,318	140,450,318	0	
Aggregate write-ins for other than invested assets	<u>167,408,219</u>	<u>40,928,175</u>	<u>126,480,044</u>	
Total assets	<u>\$2,161,973,375</u>	<u>\$336,250,844</u>	<u>\$ 1,825,722,531</u>	
<u>Liabilities, Surplus and Other Funds</u>				
Known claims reserve			\$ 76,283,098	(4)
Statutory premium reserve			600,602,037	
Other expenses			198,947,129	
Taxes, licenses and fees			9,363,141	
Current federal and foreign income taxes			683,126	
Premiums and other considerations received in advance			48,232,239	
Amounts withheld or retained by company for account of others			597,917	
Payable to parent, subsidiaries and affiliates			53,052,422	
Aggregate write-ins for liabilities			<u>91,915,956</u>	
Total liabilities			\$ 1,079,677,065	
Common capital stock		\$200,000,000		
Unassigned funds (surplus)		<u>546,045,466</u>		
Surplus as regards policyholders			<u>746,045,466</u>	
Total liabilities, surplus and other funds			<u>\$ 1,825,722,531</u>	

Operations and Investment Exhibit
for the Year Ended December 31, 2004

Statement of Income

Operating Income

Title insurance premiums earned	\$ 3,280,374,630
Escrow and settlement reserves	186,252,642
Other title fees and service charges	<u>96,844,673</u>

Total operating income 3,563,471,945

Deduct:

Losses and loss adjustment expenses incurred	\$ 127,139,570
Operating expenses incurred	<u>3,324,844,245</u>

Total operating deductions 3,451,983,815

Net operating gain 111,488,130

Investment Income

Net investment income earned	\$ 78,887,047
Net realized capital gains	<u>655,338</u>

Net investment gain 79,542,385

Net income before federal income taxes	191,030,515
Federal and foreign income taxes incurred	<u>60,505,157</u>

Net income \$ 130,525,358

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2003 \$ 746,580,611

Net income	\$ 130,525,358
Net unrealized capital losses	(137,244,713)
Change in net deferred income tax	27,220,294
Change in nonadmitted assets	(98,276,850)
Aggregate write-ins for gains and losses in surplus	<u>77,240,766</u>

Change in surplus as regards policyholders for the year (535,145)

Surplus as regards policyholders, December 31, 2004 \$ 746,045,466

Reconciliation of Surplus as Regards Policyholders
from December 31, 2000 through December 31, 2004

Surplus as regards policyholders, December 31, 2000,
per Examination

\$406,777,064

	<u>Gain in</u> <u>Surplus</u>	<u>Loss in</u> <u>Surplus</u>
Net income	\$611,106,511	\$
Net unrealized capital losses		181,790,856
Change in net deferred income tax	25,271,862	
Change in nonadmitted assets		146,304,327
Cumulative effect of changes in accounting principles	72,266,972	
Capital changes: Transferred from surplus (Stock Dividend)	100,000,000	
Surplus adjustments: Transferred to capital (Stock Dividend)		100,000,000
Dividends to stockholders		100,000,000
Aggregate write-ins for gains in surplus	<u>58,718,240</u>	<u> </u>
Total gains and losses	<u>\$867,363,585</u>	<u>\$ 528,095,183</u>

Increase in surplus as regards policyholders

339,268,402

Surplus as regards policyholders, December 31, 2004,
per Examination

\$746,045,466

COMMENTS ON FINANCIAL STATEMENT

(1) Common Stocks

The Company is not in compliance with the Securities Valuation Office (SVO) Manual because it failed to report its 2004 subsidiary purchases to the SVO within 30 days of the acquisition or formation of the subsidiary. It was recommended that the Company comply with Part Eight, Section 1 of the NAIC SVO Purpose and Procedures Manual. In November 2005, the Company started filing some of its non-insurance subsidiary common stocks that were acquired in 2004 with the SVO.

(2) Mortgage Loans on Real Estate

The Company is not in compliance with California Insurance Code Section (CICS) 1100. One of the mortgage loans reported on Schedule B, Part 1, which accounted for 97% of the total mortgage loan book value reported in the Annual Statement, represented various notes receivables that a lender in San Bernardino assigned and transferred all of its rights, title and interest to one of the Company's subsidiaries, The Inland Empire Service Corporation. The notes were secured by deeds of trust. The notes receivables did not substantiate any ownership interest of the Company. It is recommended that the notes receivables be under the name of the Company or that the Company should substantiate any ownership interest on the notes receivables to comply with CICS 1100.

(3) Receivable from Parent, Subsidiaries and Affiliates

The Company has an underwriting agreement with First American Title Company (FATCO). The agreement stated that FATCO remits to the Company on or before the 15th day of each calendar month the total amount of fees for title policies issued through its offices during the preceding calendar month. Based on the review of the account, the account balance was not being settled according to the terms of the agreement. It is recommended the Company comply with its own underwriting agreement by implementing procedures to settle the balances on a regular basis. The Company implemented a procedure wherein a monthly entry will be posted to the general ledger for the payment of underwriting fees due to the Company. It will be recorded as a cash payment by

FATCO with an offset to the intercompany payable account, and accordingly, the opposite entry will be booked by the Company.

(4) Known Claims Reserve

The Company obtained an actuarial opinion from its consulting actuary, Milliman, Inc., attesting to the adequacy of its loss reserves as of December 31, 2004. This report was reviewed by a Casualty Actuary from the California Department of Insurance, and based on the review the Company's reserves were accepted for purposes of this examination.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

Accounts and Records – Escrow Accounts (Page 14): It is recommended that the Company resolve all the outstanding escrow balances before it closes the escrow account and escheat undisbursed escrow funds as unclaimed property in accordance with the requirements of each state.

Account and Records – Custodial Agreement (Page 14): It is recommended that the Company comply with California Insurance Code (CICS) Section 1104.9(a)(1).

Comments on Financial Statement – Mortgage Loans on Real Estate (Page 19): It is recommended that the Company comply with CICS 1100.

Previous Report of Examination

Accounts and Records – Custodial Agreement (Page 12): The custodial agreement in force as of December 31, 2000 was not in compliance with the requirement of CICS 1104.9(d). The Company is still not in compliance.

ACKNOWLEDGEMENT

The courtesy and cooperation extended by the Company's officers and employees during the course of this examination are hereby acknowledged.

Respectfully submitted,

_____/S/_____
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